

**EXECUTIVE SECRETARIAT**  
ROUTING SLIP

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		ACTION	INFO	DATE	INITIAL
1	DCI		X (w/o att)		
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3	EXDIR				
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14	D/PAO				
15	D/PERS				
16	VC/NIC	X (w/o att)			
17	NIO/USSR		X (w/att)		
18	D/SOVA		X (w/o att)		
19	ES		X		
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SUSPENSE

30 April 1986

Date

Remarks

To 16: NIO/USSR to get back to DCI re CSIS speech and also re any comments on Summit approach and differences between Harry Rowen and SOVA.

Executive Secretary

23 April 1986

Date

3637 (10-81)

Executive Registry

86- 1729

22 April 1986

MEMORANDUM FOR: National Intelligence Officer for USSR

FROM: Director of Central Intelligence

SUBJECT: 16 May CSIS/Georgetown Speech and Tokyo Summit

1. Henry Kissinger got me to give a talk at Georgetown on 16 May on the Soviet Union. The attached speech was prepared for me. I haven't read it but, on the basis of past experience, I would not think I'd be inclined to use it. I'd appreciate receiving some of the things you have been saying in your talks. After I look at it, let's have a talk about what I might want to say on 16 May.

2. We had a meeting at the White House on the Tokyo Summit today. The Summiteers are to select one or two subjects for general discussion. One is how to handle a wounded bear; the other is world agriculture. There seems to be a strong tendency among the Summiteers to choose world agriculture as the subject for discussion, in part because it may lead to some practical policy issues.

3. Also at the Tokyo Summit meeting, Allen Wallis talked to me about the Rowen presentation. Judging from Harry's article in the WALL STREET JOURNAL on 21 April and what Wallis had to say, I don't see the disparity between what the President heard from Allen and what he heard from us at as much variance as the SOVA fellows seem to think.

4. I am returning your memo on the Ogarkov paper which I read, along with a copy of Harry Rowen's WALL STREET JOURNAL piece.

  
William J. Casey

## Attachments:

1. CSIS Speech Folder
2. Eyes Only Envelope on The Evolution of Soviet Strategy and Military Policy
3. WSJ Article by Harry Rowen, 21 April 1986

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THE WALL STREET JOURNAL MONDAY, APRIL 21, 1986

# Gorbachev and the Ailing Russian Bear

By HENRY S. ROWEN  
And VLADIMIR G. TREML

The leadership of the Soviet Union is confronted with the most fundamental and difficult of choices, one made more urgent by the precipitous decline in oil prices:

- It faces the prospect of continued, perhaps worsened, economic stagnation. Overcoming this condition requires a major increase in the productivity of labor and capital; this increase is sought through new managers, more discipline, a crackdown on alcoholism, and renovation of the nation's stock of machinery. But what is really needed is to reduce the regime's central control over the economy.

- Reduced control would alter the distribution of income, transform repressed inflation into open inflation and probably cause labor strife. In time, it would diminish party control over the country.

- Without such a shift the country is fated to remain economically backward—behind by about a generation (25 to 30 years)—relative to the West. Although such a lag certainly doesn't exist for the Soviet military sector today, over time its ability to compete militarily will be in jeopardy.

It is increasingly apparent that the period of rapid economic growth from 1950 to 1975, which averaged 5% a year, was a one-time shift from a very backward, largely agricultural society to a semi-modern, largely industrialized one. This growth was achieved through extensive exploitation of natural resources, more labor inputs, and technology obtained from the West. Since 1975, estimated gross national product growth has averaged a little more than 2% a year (1% per capita). Although growth in the West also slowed over this period, the West was badly hurt by oil-price rises while the Soviet Union, a major oil and gas exporter, profited from them.

## No Call for Sacrifices

There also is abundant evidence of grave social ills. Infant mortality has been increasing, alcoholism has reached alarming levels, and life expectancy has been declining for 20 years. By 1980, the average life expectancy of men had receded to the mid-1950s level of about 60 years.

The new Five Year Plan (1986-90) promises to get the country moving again. It sets an ambitious target of 5%-a-year growth to 2000. It calls for a more modest 3½% GNP increase for the next five years, industrial output growing at 4½% a year and machinery output at around 7%. The supply of consumer goods is to grow also; there was no call for sacrifices at the recent 27th

This is to be done with little more labor input and an increase of less than 4% a year in total investment. A huge investment increase is planned for machine building (80%) and a large one for energy (about 30% for oil, coal and electric power). The large share going to agriculture is to be held nearly constant. So all other categories will have to fall: transportation, construction, housing, services. The key, then, must be increased productivity. Factors of production (of labor and capital), which declined about 1% a year after 1975, are now to increase by almost 1% a year.

This is not a credible plan. An obvious problem is a much worsened trade prospect. Since the early 1970s the Soviet economy has become much more dependent upon trade; there have been massive imports of food, consumer goods and machinery. (By the early 1980s more than one-third of newly installed machinery was imported.) Now, that growth source is gone. After years of increases, oil production has declined for two years and in 1985 the volume of oil exports to the West declined 30%. To compound the problem, the dollar price of oil has fallen about one-half. (This drop lowers the value of natural gas sold to Western Europe about \$1.5 billion a year; if the Europeans don't negotiate a payment cut, they will be giving the Soviets a huge gift.) To top it off, weapons sales to oil-rich countries, a market recently valued at \$5 billion to \$6 billion a year, are shrinking fast.

Altogether, Soviet hard-currency earnings in 1986 will be half what they were in 1984. Moscow's response last year was to borrow an additional \$5 billion, and it will seek more this year. By the end of 1986, its net debt probably will be about \$20 billion as against annual hard-currency earnings of under \$20 billion. Further borrowing from private sources will come harder—in the absence of Western government guarantees. Moscow will try to sell more oil to the West, perhaps diverting more from the East Europeans for that purpose, and more gold and diamonds, but if oil prices stay down, it won't come close to recouping its losses.

The result will be a sharp fall in some combination of Soviet food and equipment imports from the West; the choice of which to cut will be a hard one. At the very least, extra machinery will not be available from the West—unless Western governments decide to bail out Mikhail Gorbachev by underwriting loans and overpaying for gas.

Moscow is already squeezing the East Europeans to get more and better machinery out of them. The days of Soviet subsidized oil are over; indeed, Moscow is now trying to get more from them in exchange for less. The limit to this squeezing process will be the fear of further popular eruptions in Eastern Europe.

In short, economic performance will probably be no better than in the recent past and could easily be worse. (The anti-drinking campaign, potentially beneficial in the long run, probably won't help soon. It leaves people with more money but few additional goods; the likely result is more inflation.) One consequence—of symbolic importance—is that Japan by 1990 may have displaced the Soviet Union as the

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world's second-largest economy.

Mr. Gorbachev talks about major changes that "ought" and "should" be made. But there is a poverty of new, basic ideas, and nothing major happens. Of course, the bureaucracy mightily resists change and Mr. Gorbachev will want to limit changes to those essential to eking out enough economic gains to enable him, above all, to keep control over the country and also to sustain its military strength and its foreign empire. With good weather, enough Western resources, and skillful management, he can defer the riskier strategy of giving people more economic freedoms in order to stimulate growth.

If the regime doesn't change course, it will gradually lag in military competition, given the constraint on resources and the evolution of modern technologies. These technologies center on the processing and transmission of information, technologies that a centrally planned system not only lags in creating but that also threaten its internal control. Moreover, the regime is not in good shape to take on costly new ventures abroad. Still, a note of caution: Operations in Afghanistan, Angola and Nicaragua are being pursued more vigorously under the new management; it won't pass up low-risk opportunities (for instance in Pakistan or Iran), and it still possesses a powerful military establishment.

Although there is much uncertainty about if and when Mr. Gorbachev will try to move toward a marketlike system and what will happen (including what will happen to him) if he tries, several things are clear: (a) The system is not on the verge of collapse; (b) the Soviet Union is not going to strike against the West—retreat is more in character for a Leninist system in difficulty, and (c) Mr. Gorbachev badly needs relief from the military competition of the West and just as badly needs the West's resources.

#### Issues to Be Aware of

What should the West do? Here are some guiding principles. First, the democracies have an interest in a politically diversified Soviet system. A judgment must be made on whether helping the ailing bear or having unsubsidized economic relations is the better way to promote this goal. Many Europeans and some Americans hold that Western subsidies keep the Soviets from becoming desperate and more dangerous, and promote useful change. That theory, in the form of détente, worked poorly in the 1970s and prospects for it now aren't good. The key reason is that the Moscow establishment doesn't want to change; the more help it gets, the less likely it is to change.

Second, all capitalist leaders should be conscious of the weakening Soviet competitive position. For the Japanese it bears on their recovery of four small Soviet-occupied islands north of Japan's mainland; for the Europeans it offers increased scope for reducing the Soviet military threat to them (without matching Western concessions); for the U.S., which has an interest in all of these issues, it bears on nuclear-arms-control negotiations, extensions of the Soviet empire in the Third World, Jewish emigration and other matters at issue.

Third, the more communication and personal contact there is between the peoples of the Soviet Union and the West—and the freer the communications among the Soviet peoples—the more constrained will be the arbitrary power of the rulers. In addition to what we unilaterally do (today with radios, tomorrow perhaps with direct TV broadcasting), promoting this purpose should be prominent in our continuing transactions with the regime.

The pressure is mounting in Moscow to travel partway down the capitalist road. Although significant movement seems unlikely soon, there may be some by the end of the decade. At a later stage in the evolution of the internal crisis, a wider range of positive Western actions to promote change might be warranted. But that is a later and uncertain prospect.

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*Mr. Rowen is a professor at the Stanford University Business School and a senior research fellow at the Hoover Institution. Mr. Trembl is a professor of economics at Duke University.*

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DCI REMARKS TO  
CSIS INTERNATIONAL COUNCILLORS

16 MAY 1986

THE USSR UNDER GORBACHEV: MORE GUNS OR NEW BUTTER?

JUST ABOUT A YEAR AGO, A NEW FACE APPEARED IN THE TOP LEADERSHIP SPOT ON THE KREMLIN WALL. AFTER A PERIOD OF POLITICALLY UNSETTLED CONDITIONS IN THE SOVIET UNION -- POLITELY REFERRED TO AS A "LEADERSHIP TRANSITION" -- POLITICAL POWER CAME TO REST IN THE HANDS OF MIKHAIL GORBACHEV [MEEK-HILE GOR-BAH-CHOFF] AND HIS SUPPORTERS. IN THE PAST YEAR WE HAVE SEEN GORBACHEV DEMONSTRATE A VIGOROUS LEADERSHIP STYLE, UNVEIL NEW DOMESTIC PROGRAMS, AND INJECT SOMETHING APPROXIMATING A NEW OPTIMISM INTO THE SOVIET BODY POLITIC. BUT DOES THE GORBACHEV ERA REPRESENT A BREAK WITH THE PAST -- SOMETHING GENUINELY NEW? OR IS IT MERELY A CONTINUATION OF THE SOVIET POLICIES AND PRACTICES OF THE PAST -- WITH ONLY A NEW VENEER?

ROBERT CONQUEST, A NOTED SOVIET AFFAIRS SCHOLAR, ONCE OBSERVED THAT "IF THE UNITED STATES HAS A MILITARY-INDUSTRIAL COMPLEX, THE SOVIET UNION IS A MILITARY-INDUSTRIAL COMPLEX." DESPITE INEFFICIENCIES IN ITS ECONOMY, AND POLITICAL SETBACKS DUE TO INFIGHTING AMONGST THE LEADERSHIP, THE SOVIETS HAVE BUILT OVER THE LAST TWENTY YEARS ARMED FORCES SO POWERFUL THAT THEY WILL ENSURE CONQUEST OF TERRITORY ON ANY BATTLEFIELD. IRONICALLY, THEY HAVE DONE THIS IN LARGE PART THROUGH THE ACQUISITION OF

....WESTERN TECHNOLOGY AND